Hawaii Technology Development Corporation
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Honolulu, Hawaii 96813 | www.htdc.org

Written Statement of
Len Higashi
Acting Executive Director
Hawaii Technology Development Corporation
before the
Senate Committee On Energy, Economic Development, And Tourism
Wednesday, February 10, 2021
3:00 p.m.
Videoconference

In consideration of
SB927
RELATING TO TAXATION.

Chair Wakai, Vice Chair Misalucha, and Members of the Committee.

The Hawaii Technology Development Corporation (HTDC) offers **comments** on SB927 that provides that up to $50,000 per year in income earned and proceeds derived from stock options or stock by an employee from a qualified high technology business, as defined therein, or an investor who qualifies for a high technology business investment tax credit, shall be excluded from taxation, provided the employee or investor is a resident of the State, and provided further that amounts in excess of $50,000 in the taxable year shall be taxed at the applicable income tax rate.

HTDC appreciates the intent of SB927 to encourage local jobs and to protect the State's limited resources under the current environment. HTDC defers to the Department on the technical aspects of this measure.

Thank you for the opportunity to offer these comments.

DAVID Y. IGE
GOVERNOR

JOSH GREEN M.D.
LT. GOVERNOR

ISAAC W. CHOY
DIRECTOR OF TAXATION

STATE OF HAWAII
DEPARTMENT OF TAXATION
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To: The Honorable Glenn Wakai, Chair;
The Honorable Bennette E. Misalucha, Vice Chair;
and Members of the Senate Committee on Energy, Economic Development, and Tourism

From: Isaac W. Choy, Director
Department of Taxation

Date: February 10, 2021
Time: 3:00 P.M.
Place: Via Video Conference, State Capitol

Re: S.B. 927, Relating to Taxation

The Department of Taxation (Department) offers the following comments regarding S.B. 927 for your consideration.

S.B. 927 provides that up to $50,000 per year in income earned and proceeds derived from stock options or stock by an employee from a qualified high technology business, or an investor who qualified for the high technology business investment tax credit is excluded from taxation, provided the employee or investor is a resident of the State. Amounts that are in excess of $50,000 in the taxable year are taxed at the applicable income tax rate. S.B. 927 is effective upon approval and applies to taxable years beginning after December 31, 2020.

The Department first notes that under current law, *all* of the income earned and proceeds derived from stock options or stock by an employee, officer, or director of a qualified high technology business, or by an investor who qualified for the high technology business investment tax credit under section 235-ll0.9, Hawaii Revised Statutes (HRS) is excluded from taxation. While it appears that the measure is creating an exemption, it is actually limiting the exemption to $50,000.

Finally, the Department notes that the restriction limiting the exemption to Hawaii residents is likely to violate the United States Constitution.

Thank you for the opportunity to provide comments.

WRITTEN TESTIMONY OF
THE DEPARTMENT OF THE ATTORNEY GENERAL
THIRTY-FIRST LEGISLATURE, 2021

ON THE FOLLOWING MEASURE:
S.B. NO. 927, RELATING TO TAXATION.

BEFORE THE:

SENATE COMMITTEE ON ENERGY, ECONOMIC DEVELOPMENT, AND TOURISM

DATE: Wednesday, February 10, 2021 **TIME:** 3:00 p.m.

LOCATION: State Capitol, Room 224

TESTIFIER(S): **WRITTEN TESTIMONY ONLY.**
(For more information, contact Kristen M.R. Sakamoto,
Deputy Attorney General, at 808-586-1470)

Chair Wakai and Members of the Committee:

The Department of the Attorney General has concerns regarding this bill and provides the following comments.

This bill amends section 235-9.5(a), Hawaii Revised Statutes (HRS), which provides an exclusion from income for Hawaii Income Tax to employees, officers, directors, and investors of qualified high technology businesses (QHTBs) for income from stock options and stock from the QHTBs. Specifically, this bill (1) adds a requirement that the taxpayer be a resident of the State and (2) limits the exclusion to $50,000.

The residency requirement in this bill may be subject to a challenge under the Privileges and Immunities Clause of the United States Constitution.

The Privileges and Immunities Clause, contained in Article IV, Section 2, of the United States Constitution, affords citizens of a state the right to "carry on business in another without being subjected in property or person to taxes more onerous than the citizens of the latter State." *Lunding v. New York Tax Appeals Tribunal*, 522 U.S. 287, 296 (1998) (quoting *Shaffer v. Carter*, 252 U.S. 37, 56 (1920)). As such, the Clause "prohibits a State from denying nonresidents a general tax exemption provided to residents." *Lunding*, 522 U.S. at 302.

To overcome a challenge under the Privileges and Immunities Clause to a law that distinguishes between residents and nonresidents, a state must demonstrate that (1) "there is a substantial reason for the difference in treatment"; and (2) "the discrimination practiced against nonresidents bears a substantial relationship to the State's objective." *Lunding*, 522 U.S. at 298 (quoting *Supreme Court of N.H. v. Piper*, 470 U.S. 274, 284 (1985)) (internal quotations omitted).

This bill provides a tax benefit (by way of an exclusion of income) to residents, while denying the same tax benefit to nonresidents. Moreover, this bill does not appear to be designed to achieve an overall "substantial equality of treatment" between residents and nonresidents.

Section 235-4, HRS, imposes tax on residents' income from sources both within and outside the State, while nonresidents are taxed only on property and business within the State. With respect to income from intangible property, including interest and dividends from stocks, said income is sourced, pursuant to section 18-235-4-08(b), Hawaii Administrative Rules, to the owner's domicile unless the property has acquired a "business situs" in the State by being "employed as capital in this State or [where] the possession and control of the property has been localized in this State." Accordingly, if QHTB stock options or stock have acquired a business situs in the State, this bill will subject income from those stock options or stock to taxation for nonresidents, while exempting income from those stock options or stock for residents.

Based on the foregoing, this bill may be subject to challenge under the Privileges and Immunities Clause. To avoid a potential constitutional challenge, we recommend deleting the provision on page 1, lines 15-16, that reads, "provided that the taxpayer is a resident of this State as defined in section 235-1;".

Thank you for the opportunity to provide comments.

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304 Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: INCOME, Limit Qualified High Tech Business Stock Option Exclusion TAXATION

BILL NUMBER: SB 927; HB 316

INTRODUCED BY: SB by WAKAI, MISALUCHA, Baker, Chang, Keith-Agaran, Shimabukuro; HB by TAKAYAMA

EXECUTIVE SUMMARY: Provides that up to $50,000 per year in income earned and proceeds derived from stock options or stock by an employee from a qualified high technology business, as defined therein, or an investor who qualifies for a high technology business investment tax credit, shall be excluded from taxation, provided the employee or investor is a resident of the State, and provided further that amounts in excess of $50,000 in the taxable year shall be taxed at the applicable income tax rate.

SYNOPSIS: Amends section 235-9.5, HRS, to so provide.

EFFECTIVE DATE: Upon approval.

STAFF COMMENTS: Section 235-9.5, HRS, was one of a suite of incentives for the high technology industry that was enacted by Act 221, SLH 2001.

Substantively, over the last decade, Hawaii adopted various tax incentives to encourage the development of high technology businesses in the state. The acts provided investment and research credits as well as income exclusions providing tax relief to high tech businesses and individuals associated with high tech businesses.

Many of the incentives provided by Act 221 were either repealed or allowed to sunset. Some, like the tax credit for research activities, live on although amended over the years. This one, the exclusion for income earned and proceeds derived from stock options or stock associated with a qualified high technology business, remains intact from the form in which Act 221 left it. The amendments proposed by this bill would limit or weaken the incentive, which would appear to be appropriate given the 20 years that have elapsed since enactment.

Lawmakers should be mindful that investments are made with the prospect that the business will yield a profit. If the prospects for making a profit are absent, of tax credits or other incentives will not attract investment from outside Hawaii's capital short environment unless investors are assured of making a profit. People do not invest to lose money. Hawaii's high cost of living, high tax structure, and extensive regulatory environment need to be addressed, in a manner that makes Hawaii genuinely competitive with other states, before Hawaii stands a chance to win a significant place in the high tech industry.

Digested 2/5/2021

LATE

2/9/2021

Jeffrey D. Hong
TechMana LLC
Honolulu, HI, 96813

Chair Wakai, Vice Chair Misalucha, and Members of the Energy, Economic Development and Tourism Committee.

As the Chief Technology Officer of a local software company I would like to provide comments on SB927. The Bill provides an opportunity to address tax incentives for High Technology Businesses in Hawaii.

The work-from-home movement driven by COVID can bring High Technology Businesses to Hawaii one worker at a time. The new limitation of $50,000 will provides a ceiling of $5,500 as an incentive for High Technology Business individuals to move to Hawaii. Should we be more aggressive with a $100K ceiling?

Most high technology employees are paid with Restricted Stock Units. This is an opportune time to include this form of compensation into the legislation.

> "Income earned and proceeds derived from stock options or stock" includes income from:
> (1) Dividends from stock or stock received through the exercise of stock options or warrants;
> (2) The receipt or the exercise of stock options or warrants; or
> (3) The sale of stock options, restricted stock units, or stock, including stock issued through the exercise of stock options or warrants.

I know many employees of Salesforce and other technology firms that have located to Hawaii during the pandemic but that have kept California as their tax domicile. Many are returning kama'aina. We need to encourage these people to make Hawaii their home.

Mahalo,

Jeffrey D Hong

Jeffrey D. Hong
Chief Technology Officer
TechMana LLC

TechMana LLC